SEPTEMBER 2012

THE UNITED STATES FURTHER EXPANDS SANCTIONS AGAINST IRAN

On August 10, 2012, President Barack Obama signed into law the Iran Threat Reduction and Syria Human Rights Act of 2012 (the "Act").[1] While the Act contains a section imposing sanctions in response to human rights abuses committed against Syrian citizens, its primary focus is on strengthening and expanding an already extensive U.S. sanctions program against Iran. This *Commentary* highlights three key areas where the Act has substantially altered the landscape of U.S. sanctions related to Iran.

U.S. PARENT COMPANIES LIABLE FOR VIOLATIONS OF SANCTIONS BY FOREIGN SUBSIDIARIES

Arguably, the Act's most significant expansion of sanctions against Iran is the inclusion of activities by non-U.S. subsidiaries of U.S. parent companies within the scope of certain sanctions that have been previously imposed against Iran by the United States. The Iranian Transactions Regulations ("ITR"), 31 C.F.R. Part 560, promulgated under the authority of the International Emergency Economic Powers Act ("IEEPA") and administered by the Department of the Treasury's Office of Foreign Assets Control ("OFAC"), have historically prohibited U.S. persons from engaging in most transactions involving Iran. Prior to the Act, the broad prohibitions contained in the ITR generally applied only to "United States persons," defined in the ITR as "any United States citizen, permanent resident alien, entity organized under the laws of the United States (including foreign branches), or any person in the United States." 31 C.F.R. § 560.314.[2] Thus, transactions by foreign-incorporated subsidiaries of U.S. parent companies have generally been outside the scope of the ITR, absent any involvement of a United States person.

1 Pub. L. No 112-158, 126 Stat. 1214 (2012). The enacted version is not yet available.

2 Section 2 of the Act adopts the definition of "United States person" provided in Section 101 of the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ("CISADA") (22 U.S.C. § 8511), but that definition in relevant part parallels the ITR.

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The Act, however, purports to broaden the scope of the ITR by requiring the President to prohibit activities by foreign-incorporated subsidiaries of U.S. parent companies, as well as other types of entities owned or controlled by the U.S. parent company or by "United States persons" in general. Specifically, the Act provides:

> Not later than 60 days after the date of the enactment of this Act, the President shall prohibit an entity owned or controlled by a United States person and established or maintained outside the United States from knowingly engaging in any transaction directly or indirectly with the Government of Iran or any person subject to the jurisdiction of the Government of Iran that would be prohibited by an order or regulation issued pursuant to the International Emergency Economic Powers Act (50 U.S.C. 1701 *et seq.*) if the transaction were engaged in by a United States person or in the United States.

Section 218(b).[3] "Entity" is defined as "a partnership, association, trust, joint venture, corporation or other organization." Section 218(a)(1). The phrase "own or control" is defined as (i) holding more than 50 percent of the equity interest by vote or value in the entity; (ii) holding a majority of seats on the board of directors of the entity; or (iii) otherwise controlling the actions, policies, or personnel decisions of the entity. Section 218(a)(2). Civil penalties as set forth in Section 206(b) of IEEPA may be imposed against a U.S. person if a non-U.S. entity that it owns or controls violates, attempts to violate, conspires to violate, or causes a violation of the prohibition. Section 218(c).[4] The penalties, however, do not apply where "the United States person divests or terminates its business with the entity not later than the date that is 180 days after the date of the enactment of this Act." Section 218 (d).

DISCLOSURE REQUIREMENTS WITH THE SECURITIES AND EXCHANGE COMMISSION ("SEC")

The Act amends the Securities Exchange Act of 1934 to require each issuer required to file annual or quarterly reports with the SEC pursuant to Section 13(a) of the Securities Exchange Act of 1934 (the "Exchange Act") to disclose if, during the period covered by the report, it or any of its affiliates had "knowingly engaged in" certain sanctionable activity under the ISA or CISADA. The Act also requires each such issuer to disclose if it or any of its affiliates had "knowingly conducted any transaction or dealing with" persons whose property had been blocked for their participation in terrorism or proliferating weapons of mass destruction, or any person identified as part of the Government of Iran "without the specific authorization of a Federal department or agency." Section 219(a) implementing a new Section 13(r) of the Exchange Act. Any such issuer must also file a notice with the SEC indicating that a disclosure has been included in a filed report. That notice is sent to certain congressional committees and to the President, who then is to initiate an investigation into the possible imposition of sanctions. In addition, the Commission is required to make the information provided in the disclosure and the notice available to the public by posting the information on the Commission web site. Section 219(a). These disclosure obligations come into effect with respect to reports required to be filed with the SEC 180 days after enactment of the Act. Section 219(b).

EXPANSION OF PETROLEUM SECTOR SANCTIONS

The Iran Sanctions Act ("ISA"), which was passed in 1996, directed the President to impose sanctions on any entity, foreign or domestic, that makes an investment of $20 million or more that "directly and significantly contribute[s] to the enhancement of Iran's ability to develop petroleum resources of Iran." Because any investment that was sanctionable under the ISA would also have been illegal if performed by a U.S.-based company, commentators have long noted that, as a practical matter, the ISA was primarily an attempt to regulate the overseas transactions of foreign firms.

3 The phrase "any person subject to the jurisdiction of the Government of Iran" has not been defined by the U.S. government, and its scope is unclear.

4 The legislative history of the Act further suggests that a U.S. parent company would be subject to penalties "if its foreign subsidiary has knowledge or should have had knowledge that the subsidiary was doing prohibited business with Iran, even if the U.S. parent company has no knowledge of these transactions." 158 Cong. Rec. S5862 (Aug. 1, 2012) (statement of Sen. Johnson).

The ISA was amended with the passage of the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ("CISADA"), such that persons engaged in the energy sector became subject to sanctions in general from, *inter alia*, selling, leasing, or providing goods or services that might directly and significantly facilitate the maintenance or expansion of Iran's domestic production of refined petroleum products; selling or providing Iran with refined petroleum products; and providing goods and services that could directly and significantly contribute to enhancing Iran's ability to import refined petroleum products. CISADA also imposed mandatory sanctions on foreign financial institutions that knowingly facilitate transactions related to: (i) Iran's weapons of mass destruction programs; (ii) Iranian support for terrorism; (iii) persons subject to United Nations sanctions; (iv) the Iranian Revolutionary Guard Corps and its affiliates; and (v) designated Iranian banks.

In addition, the National Defense Authorization Act for Fiscal Year 2012 ("NDAA"), signed into law on December 31, 2011, added significant additional prohibitions and restrictions on Iran's financial sector as part of the increasing effort to isolate Iran from the global economy, including prohibiting or imposing strict conditions on foreign financial institutions attempting to open or maintain a correspondent or a payable-through account where those institutions knowingly conduct significant transactions with the Central Bank of Iran or designated Iranian financial institutions.

The Act expands these laws in a variety of ways. For example, the Act purports to expand the scope of the ISA by subjecting to sanctions any person who knowingly sells, leases, or provides to Iran goods, services, technology, or support above threshold levels that could directly and significantly contribute to the maintenance or enhancement of Iran's ability to develop petroleum resources located in Iran or its domestic production of refined petroleum products. This includes any direct or significant assistance with respect to the construction, modernization, or repair of petroleum refineries or related infrastructure, such as the construction of roads, railways, and ports used to support the delivery of refined petroleum products. Section 201.

The Act also, for example, targets persons who own, operate, control, or insure vessels used to transport crude oil from Iran (Section 202); adds three sanctions to the available sanctions under the ISA (bringing the total to 12 available sanctions) (Section 204); and now requires the President to impose at least five of the available sanctions upon any person determined to have engaged in activities as set forth in Section 5 of the ISA. Sections 201-203.

In addition, the Act amends the NDAA by eliminating an exemption from sanctions for state-owned banks that did not engage in transactions involving the sale or purchase of petroleum or petroleum products to or from Iran. Section 504. There was also an exemption to the NDAA's sanctions if the President determined that the country with primary jurisdiction over the foreign financial institution had significantly reduced its purchases of Iranian crude oil. The Act amends the NDAA such that any country that has received an exemption for reducing its purchases of Iranian crude oil must reduce its purchases from Iran to zero for its financial institutions to continue to receive the exemption. Section 504.

CONCLUSION

U.S. companies that have had foreign subsidiaries doing business in Iran are now under a tight deadline to put a stop to those activities or risk sanctions under this latest Act. The Act also significantly enhances the disclosure obligations of U.S. issuers for activities related to Iran, both increasing the likelihood that any activities that are covered by the ISA will be investigated, and where the activities do not relate to the ISA, increasing the potential reputational harm for engaging in activities that are legal under U.S. law. The Act also strengthens the sanctions program targeting Iran's oil and gas industry, increasing the scope of activities potentially sanctionable. In addition to these significant changes, the Act also makes numerous incremental additions to the Iranian sanctions regime, all of which serve to increase the risk of exposure to sanctions.

U.S. companies that own or control entities engaging in dealings with Iran, issuers in U.S. markets with Iranian operations, and non-U.S. companies in the oil and gas sector should all take a close look at the latest sanctions and ensure that their compliance programs are updated and adequate to the task.

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